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MEMORANDUM

THE WHITE HOUSE

WASHINGTON

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TO: Hamilton Jordan

FROM: Landon Butler

DATE: March 18, 1979

SUBJECT: Teamster Negotiations

Background

--A week and a half ago, in Florida, the Teamsters put economic demands on the table which seriously exceeded the inflation guidelines; the employers responded last Monday by rejecting the Teamster demands outright, and stating publicly that they intend to seek a settlement within the guidelines.

--Following the rejection by the employers, both Fitzsimmons and the employers agreed that they had reached an impasse, and jointly requested the services of Wayne Horvitz, the Director of the Federal Mediation and Conciliation Service.

--On Thursday, Fred Kahn stated publicly that the guidelines have always been intended as "trigger points" which would indicate the presence of market restrictions in a given industry: therefore, if the Master Freight agreement exceeded the guidelines, sweeping de-regulation would be appropriate. Fred made his statement with the approval of Shultz, Strauss, Gentry, Bosworth and myself. The President approved Fred's talking points in advance.

--This Monday, the negotiations will move from Florida to Washington, with Wayne Horvitz in charge; we can expect heavy media coverage.

Strauss, Gentry, Bosworth, Horvitz and I have been following the Teamster negotiations very closely for the past six weeks. All of us agree that the current situation is probably not as dire as it appears, and that there is a reasonable chance (50-50) that the negotiations will produce a settlement that is close to the guidelines.

With this background in mind, we should proceed as follows:

--Gentry and I will stay in close touch with Horvitz, who in turn will be meeting with the parties. Jack and I will keep the President, Ray, Strauss, Fred, Charlie, and the White House senior staff up to date on the progress of the negotiations.

--During the period between now and March 31 (when the contract expires), the President should not be seen as being heavily involved in the Administration's response to the negotiations. If possible, the President should take visible action on the price side of the wage-and-price program. I will stay in touch with Jody to enable him to give appropriate press responses.

--Ray should not be front-and-center in these negotiations. Ray has, correctly, taken stiff enforcement action against the Teamsters' Central States Pension Fund. If Ray is heavily involved in the Administration's effort to keep the settlement within the guidelines, we will be accused of using our law enforcement powers to obtain compliance with the anti-inflation program. Our chances for an acceptable outcome will be improved if Ray remains in the background.

The next two weeks will probably be tense; the Teamster negotiations will be portrayed as a do-or-die test of the anti-inflation program, and there will be extensive media interest. I think we are well-prepared and well-positioned; our success will depend on our ability to maintain a firm and steady course.

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

March 18, 1979

TO: The President

FROM: Fran *Fran*

RE: Speech in Dallas

Rafshoon recommends strongly that you use the basic SALT II speech originally planned for Georgia Tech for your address before the National Association of Broadcasters Convention in Dallas next Sunday.

It will need some modification but, if you approve, they will have a draft for you Tuesday.

✓ approve ______ disapprove

Told Jerry by phone
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THE WHITE HOUSE

WASHINGTON

March 18, 1979

MEMORANDUM FOR: THE PRESIDENT

FROM: STU EIZENSTAT Stu

SUBJECT: CRUDE OIL PRICING

You asked for my views on domestic crude oil pricing. This memorandum describes my recommendation -- which was arrived at after lengthy consultations with Members of Congress, labor, producers, consumers, and political advisers such as Loyd Hackler and Harry McPherson. It is different from the four proposals described in the memo sent to you on Friday.

THE OPTION

This approach has four basic elements:

- establish a "world incentive price" at a level equal to the current world posted price which rises with the rate of inflation thereafter. This price is the maximum which U.S. producers may receive, thereby serving as a cap on the extent to which U.S. prices follow OPEC's. It protects the economy against the effects of a substantial future OPEC price increase.

- permit oil produced from deep strippers (also called marginal wells) and enhanced recovery projects (use of secondary or tertiary recovery techniques) to receive the world incentive.

- permit the price of newly discovered oil to rise to the world incentive price.

- retain price controls on that upper and lower tier oil which does not qualify for one of the above incentives. Permit these price categories to rise with the rate of inflation. (Note: certain regulatory changes in the decline rate for old oil which everyone agrees needs doing would be made.)

It is similar in approach to Option 3 described in the Friday memo except that it is considerably more generous in the new production inventives provided, and it sets a cap on the extent to which U.S. prices are automatically permitted to follow the world level. It does not contain a tax since only oil which requires a new incentive to maximize production is increased, and the cap prevents windfalls which would otherwise result from OPEC increases. It will, however, require legislation in 1981 to extend the cap and the upper and lower tier controls.

While I do not yet have firm estimates from DoE, staff estimates that this approach would have the following effects:

- By 1981, about half of the total volume of oil now controlled in the lower tier or old oil category would be receiving the world incentive price through either the stripper or the tertiary provisions.
- By 1981, about one-third of new or upper tier oil would similarly receive the world incentive price.
- All newly discovered oil would receive the world incentive price.
- Controls would remain on a naturally declining volume of old oil; and two-thirds of upper tier oil.

Rough estimates of the CPI, supply effects under the $1.50 OPEC price increase case are:

	1979	1980	1981	1982
CPI	+.15	+.2	+.25	+.25
Import reductions (millions of barrels)	-.16	-.38	-.50	-.70

The macoreconomic and supply effects for 1979-1981 are similar to those of Option 2 from the Friday memo. Major differences from Option 2 are the amount of increase in producer revenues and thereby, the need for a tax.

ADVANTAGES OF THIS APPROACH

1. You can do it all administratively. Since no tax is necessary, you avoid engaging in a Congressional battle whose outcome is uncertain at best. A proposal which is either conditioned upon, or contains tax will, I believe, lessen the force of your decision. Al Ullman told me yesterday that he doubted whether even the OPEC or arbitrage tax could be passed (and I do not think this tax is enough to protect you politically if you select an immediate or phased decontrol approach). If you propose a tax and it fails, you will be blamed for letting the oil companies receive profits which having proposed a tax are, by definition, windfalls.

2. It provides very generous, though targetted, incentives for new production. The design of both the stripper well and the enhanced recovery incentives is based on recommendations made by producers and their Congressional representatives. My conversations with Senators Boren, Bentsen and Johnson and with a number of independent producers make me optimistic that they will support you if you follow this approach. While the major oil companies and some of the "die-hard" independent producers will be critical, you will have enough active producer support to fend off criticism for being anti-production.

3. It is generous enough to prevent a Congressional override of your decision, though attempts will still be made. It will satisfy Jim Wright on strippers and Lloyd Bentsen on enhanced recovery. Democratic producer state Members should applaud it and will help save off a Republican-lead effort to decontrol legislatively.

4. By retaining controls on upper and lower tier oil, and by establishing a price cap, it provides you with a response to those who believe that decontrol is absolutely wrong because it places our energy prices in OPEC's hands and gives all the rewards to producers. While you would be criticized from the left for being too generous you have an answer to that charge -- you have provided incentives only in those areas where new domestic production will result and you have limited the extent to which U.S. prices are vulnerable to the whims of OPEC. I believe that this will be an enormous help in explaining how your crude pricing decision is consistent with your anti-inflation drive, and will provide significant political benefits to you in the northeast and midwest in 1980. It should ease -- though not solve -- our difficulty in asking for union restraint

in upcoming wage negotiations in the face of rising energy prices.

5. It shows you putting U.S. interests first -- not letting our economy bow to either OPEC price decisions or pressure from other countries to take the lid off U.S. energy prices. I continue to sense that people are uncomfortable about making major changes in the U.S. economy just because foreign countries say we should do so.

The major disadvantages of this approach are:

1. It requires continuation of the current regulatory control program and the entitlements system. However, the complexity of the regulatory program will decrease as more and more oil moves out from controls to the world incentive price. The entitlements system will continue, though it does not require large federal resources to administer.

2. It requires backing away from the Bonn pledge, which would have to be explained on the basis of much larger than anticipated OPEC price increases, substantial pressure on the world oil market because of the Iranian disruption, and a surge in domestic inflation rates.

3. It is uncertain how this proposal would be received by the international exchange markets, which have pressed for decontrol. The effects on the dollar could be negative, but it is difficult to tell whether this will be permanent. If we have time to line up support from the independent producers, a favorable reaction from them could help the exchange market problem.

4. It will be criticized by the Republicans, by some producer state interests, and by those editors who have called for decontrol. They will claim that you have missed a chance to end the control system which impedes production at a time when domestic supplies are essential. This option does, however, provide for a very substantial part of the supply response which might be expected from decontrol by providing the world incentive price for those categories of oil where higher prices are needed for new production. The concept of a world incentive price was suggested by Senator Boren and, independently, by Jack Warren, one of the largest Texas independent producers. They feel that a cap helps protect you politically from charges that we are hooking a substantial sector of the U.S. economy to a cartel whose price determinations are only imperfectly related to normal supply and demand considerations.

While I do not believe that we need to spend much time on Monday discussing the details of this approach, the basic questions of whether to impose a cap instead of an OPEC tax, and whether or not to continue controls in order to prevent windfalls is important, both substantively and politically. Oberall, I believe that this apprach gives us the best of both worlds, given a very unpleasant series of choices.